Before the

FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on	)	**CC Docket No. 96-45**
	)	
Universal Service	)	
	)	
Multi-Association Group (MAG) Plan	)	
For Regulation Of Interstate Services	)	
Of Non-Price Cap Incumbent Local	)	**CC Docket No. 00-256**
Exchange Carriers And Interexchange	)	
Carriers	)	

COMMENTS OF NRTA AND OPASTCO

The National Rural Telecom Association (NRTA) and the Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO) submit these joint comments in response to the Further Notice of Proposed Rulemaking (FNPRM) in the above-captioned proceedings, released May 23, 2001.[1] Together, the Associations represent the majority of small and rural incumbent local exchange carriers (ILECs).

I. Introduction and Summary

The Commission sought comments on the need for, and suggested alternatives for, preventing excessive growth in universal service support for high cost, rural and insular areas

[1] Federal-State Joint Board on Universal Service; Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, *Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256*, FCC 01-157, released May 3, 2001 (FNPRM).

served by rural carriers during the five years of its concurrently-adopted interim support plan.[2] The impetus for the FNPRM was the Commission's rejection of the Rural Task Force (RTF) and Joint Board proposal to freeze ILEC and CLEC support when a competitor provides service in a rural ILEC's service area. The intention of the proposal was to prevent excessive growth in universal service funding owing to the "capture" of ILEC customers by competitive eligible telecommunications carriers (CETCs). The Commission correctly decided that the threat of excessive fund growth from changes in ILECs' per-line support when CETCs capture ILEC lines during the relatively short period of the interim rural support plan is speculative. It should refrain from adopting a remedial freeze of ILECs' support to remedy a problem that is not caused by excessive support to the ILEC. Instead, the Commission should deal directly with the real cause of the growing excessive universal service support burden on the nation's interstate ratepayers: the unlawful use of ILECs' per-line costs to measure the support payable to CETCs with different costs and characteristics.

Accordingly, the Commission should begin at once to prevent interstate customers from shouldering too high a support burden by monitoring universal service support levels due to CETC qualification for per-line support. At the same time, the Commission should fulfill its duty to ensure rigorous and effective state enforcement of the statutory mandate that support must be used only for its intended universal service purposes.[3]

The Commission should also adopt a longer term solution that will remove the source of the excessive ratepayer support burden. The Commission can only rectify the problem of excessive CETC support by limiting support for CETC's to their own costs for providing the

---

[2] *Id. a*t ¶¶ 207-211.

[3] 47 U.S.C. § 254(e)

universal services within the Commission's definition. Until the proper measure of support for CETCs is established, existing flaws and gaps in the Commission's policies for CETC support will result in uneconomic incentives to seek ETC designations and, consequently, in excessive and growing costs to interstate customers. Changes are necessary to deal with the problem of excessive growth in support for CETCs not only from the impact of line "capture" on portable per-line support, but also from practices that currently provide CETCs with support for pre-existing and "new" lines. The problem will grow as additional CETCs respond to the incentive to draw ILEC-based per-line support in rural areas.[4]

Thus, NRTA and OPASTCO urge the Commission to deal directly with the problem of excessive funding for CETCs at interstate ratepayers' expense by changing policies that distort market entry incentives and encourage uneconomic competitive entry. Above all, the Commission must develop limitations for CETC funding that will not jeopardize ILECs' ability to carry out the carrier of last resort responsibilities imposed solely upon incumbents.

II. Until It Can Remedy the Flawed CETC Support Regime, the Commission Should Refrain from Adopting a Freeze on ILEC Support When a Competitor Enters a Rural Carrier's Area and Ensure Enforcement of Section 254(e).

There is no current need for action to control the growth of ILEC support, especially via a freeze that would further cramp the already-capped support for incumbent universal service providers seeking to upgrade their networks to bring advanced services to their areas. The Commission recognized that the possibility of excessive fund growth from the capture of ILEC lines, which was identified as the potential harm against which the RTF recommendation was directed, was speculative.[5] While it recognized the purpose of the additional freeze proposed by

[4] There is no limit on the number of additional ETCs a state may designate and all may currently draw the ILEC's per-line support for all their lines in the designated area.

[5] *Id.* at ¶ 126.

the RTF, the Commission was not even able to predict the potential level of excessive fund growth when CETCs capture lines from an ILEC during the next five years.[6] The Commission also acknowledged that the indexed cap on the high cost loop fund for ILECs operates as a check on excessive fund growth.[7]

The Commission expressed its greatest concern over the fact that a freeze "may have the unintended consequences of discouraging investment in rural infrastructure…."[8] In support of its concern, the Commission cited numerous comments from carriers stating that their ability to obtain necessary support for investing in rural plant would be hampered by a freeze of loop support. The concern for such constraints on beneficial investment remains valid and will not dissipate over the next several years. The Commission should not adopt a freeze on incumbents' support, a proposed solution that does not address the true causes of excess CETC support. The costs of adopting a freeze on all ETCs' per-line support of the sort proposed by the RTF and rejected by the Commission at this time continue to "significantly outweigh" the potential benefits.[9]

However, basing CETC support on ILECs' per-line support creates an urgent need for supervision and enforcement of how the CETCs use their support. Accordingly the Commission should take immediate steps to assure itself that states are applying and effectively enforcing the provisions of Section 254(e) of the Communications Act of 1934, as amended,[10] with respect to carriers whose support is not based on their own costs. That provision requires that CETCs use

[6] *Ibid.*

[7] *Ibid.*

[8] *Id.* at ¶ 129.

[9] *See id.* at ¶ 130.

[10] 47 U.S.C. § 254(e).

universal service support "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."[11] As discussed below, the costs of ILECs and CETCs will almost certainly vary and, to the extent that a CETC receives loop support based on different, higher ILEC costs, then the CETC receives funds that exceed its own universal service costs, in violation of Section 254(e). Any overpayments while CETCs draw support based on ILEC costs will require proper attention and adequate enforcement.

III. If a CETC is Designated in a Rural ILEC's Area, Its Support Should Be Based on Its Own Costs, and It Should Receive Support Only for Lines that It Captures or Adds Following Its Designation

Rather than imposing an additional unwarranted freeze on ILECs' support, the Commission should reform its rules to ensure that, as CETCs proliferate, their support does not exceed their own universal service costs. A freeze based on the RTF proposal would inappropriately deprive ILECs and their customers of support for actual universal service and carrier of last resort costs the ILECs have already incurred. In contrast, the current rules provide CETCs with a mirrored level of support for which no need has been shown.

In the FNPRM, the Commission expressed concern regarding potential excessive growth of the high-cost loop fund. The Commission accurately noted that support for CETCs is not covered by the fund's cap on support to ILECs.[12] However, the Commission did not recognize that its rules create an opportunity for regulatory arbitrage. Specifically, the rules provide the possibility of granting ILEC-based per line support to competitive entrants in excess of their costs, providing them with the incentive and ability to pursue inefficient competitive entry.

[11] *Ibid.*

[12] *FNPRM* at ¶¶ 207, 209.

There is no basis upon which to presume that CETCs and ILECs have the same costs or that providing identical support will provide each CETC the "sufficient," but not excessive, support required by Section 254 (b)(5) of the Act. Section 254 also provides that federal universal service support mechanisms should be "specific"[13] and "predictable."[14] The Commission has stressed that CETC support must be identical to the ILEC's support, rather than "specific" to the CETC's costs and circumstances, in the name of "competitive neutrality." However, ILECs and CLECs are not similarly situated.

Only the CETC can choose whether to provide service and under what rates and terms, based on its own costs and the available per-line support based on the actual costs which each ILEC has incurred. Beyond that, under section 214 (e), a CETC is also free to provide service by reselling a rural ILEC's highest cost loops, for example, which it may acquire at prices reduced by the ILEC's universal service support. Moreover, since many ETCs utilize wireless technology, it would be an unusual coincidence for a CETC to need federal loop, switching and Long Term Support payments based on the costs of ILEC facilities and functions for the "provision, maintenance, and upgrading of facilities and services." In addition, when a carrier that has been successfully providing self-supporting service in a rural ILEC's area at market-based rates gains CETC status, the carrier draws support for all of its existing lines, rather than for the new and captured lines gained through the used of federal support.

Awarding a CETC the ILEC's per-line support also enables the CETC to seek and obtain support only where the support will give it a competitive advantage over the ILEC. Thus, when

[13] 47 U.S.C. § 254 (b)(5) and (c).

[14] 47 U.S.C. § 254(b)(5).

CETCs respond to the regulatory incentives created by the Commission's existing portability rules, CETCs' per-line costs are most likely to be lower than incumbents' costs.[15] While it is theoretically possible that a competitive carrier could have higher per-line costs than an incumbent, it is doubtful that such a competitor would choose to enter a market under those conditions. Equal support for carriers with significantly different costs, incentives and responsibilities is the opposite of competitive neutrality, which the Commission has adopted as a goal.

Moreover, the ILEC's cost per line for its carrier of last resort network increases as it loses lines to a CETC, as the FNPRM observes.[16] In contrast, the economies of scale available to the CETC may well lower its cost per subscriber as it adds lines captured from the ILEC or new lines.[17] In other words, as the ILEC's per-customer cost rises, a CETC's per-customer cost is likely to fall. Yet, due to the ILEC's increased cost per customer, based on previously incurred costs that do not disappear simply because the ILEC loses customers to the CETC, the CETC receives <u>more</u> support under the present system as its unit costs are going down. Thus, while it is essential for the ILEC -- as the carrier of last resort -- to receive increased per-line support as it loses customers to avoid stranded investment, that increased per-line support translates into pure windfall in the hands of the competitor. These increased support payments to CETCs unnecessarily increase the size of the federal universal service fund, create expensive market

---

[15] The Associations are not suggesting that support should not be portable, as the Act requires once a state has designated a CETC in a rural carrier's area. The concern is that the statute does not require portable support in an equal amount to a CETC unless its costs justify that support level.

[16] The FNPRM correctly notes that because an ILEC must recover its fixed costs from fewer lines when it loses subscribers to a competitor, its cost per customer increases. FNPRM, para. 207.

[17] If the CETC's cost structure is at all similar, its cost per customer will decrease.

distortions, unnecessarily burden the nation's ratepayers and allow the CETC to cross-subsidize its competitive services in violation of section 254(k).

In summary, providing CETCs with support based on ILEC per-line costs results in exactly the sort of excessive interstate ratepayer burden section 214(e)'s limitation on the use of support is intended to avoid. Therefore, the Commission should address excessive funding caused by CETC entry by basing CETCs' support on their own costs, instead of providing them with the same per-line support received by the ILEC, necessary for incumbents to sustain service meeting the higher standards imposed on them as carriers of last resort.[18] Limiting CETCs' per-line support to CETCs' own per-line costs would be far more consistent with the Commission's goals of competitive neutrality, encouraging investment in rural infrastructure and promoting efficient competitive entry.[19] Cost-based CETC support would also comply with Section 254(e) of the Act.

IV. Conclusion

The Commission correctly decided that the costs of imposing a freeze on ILEC and CETC support when a competitor enters a rural incumbent ETC's service area outweigh the benefits. Its decision will continue to remain reasonable and valid for the duration of the interim support plan. The Commission has a legal obligation to prevent excessive support burdens on interstate ratepayers that requires enforcement of the mandate for proper use of support. Because of the ratepayer burdens and faulty market incentives of the current portability rules, the

[18] The Commission has denied states the authority to impose the same carrier of last resort requirements on CETCs that they impose on ILECs. The Commission has also held that "… a telecommunications carrier's inability to demonstrate that it can provide ubiquitous service at the time of its request for designation as an ETC should not preclude is designation as an ETC." (In the Matter of *Federal-State Joint Board on Universal Service: Western Wireless Corporation Petition for Preemption of an Order of the South Dakota Public Utilities Commission*, CC Docket No. 96-45, FCC 00-248, para. 17 (rel. Aug. 10, 2000).

[19] *Id.*¶ 210.

Commission should change them to limit CETC support to actual CETC high costs and deny support to a carrier's self-supporting, market-based lines in service at the time the CETC qualifies as an ETC. Accordingly, NRTA and OPASTCO urge the Commission to

- watch closely that states vigorously and effectively enforce the §254(e) restriction on the use of support payments,
- refrain from adopting a further freeze on ILECs' support to curb excessive support growth for CETCs, and
- take further appropriate action to control the unjustified growth of CETC support by ensuring that a CETC's support does not exceed its own costs.

Respectfully submitted,

NRTA

By____

Margot Smiley Humphrey

HOLLAND & KNIGHT LLP
2100 Pennsylvania Avenue, N.W.
Suite 400
Washington, D.C. 20037
(202) 457-5915

OPASTCO

By_____________________________________

Stuart Polikoff
Stephen Pastorkovich
Jeffrey Smith
21 Dupont Circle, N.W.
Suite 700
Washington, D.C. 20036
(202) 659-5990

July 30, 2001

WAS1 #998238 v1